New York Tax Department Formally Proposes Corporate Tax Reform Regs

Posted on Aug. 10, 2023

By Emily Hollingsworth

The New York State Department of Taxation and Finance is moving closer to the adoption of its corporate tax reform regs after officially releasing the proposed rules for public comment.

The regulations have been formally proposed under the State Administrative Procedure Act (SAPA). The department published the proposed regs in full on its website and an overview of the regs in the August 9 *New York State Register*.

The proposed business corporation franchise tax, banking corporation franchise tax, and insurance corporation franchise tax rules reflect the 2015 overhaul of the state's corporate tax, which the department said in the *Register* "represents the most extensive restructuring of New York State's corporate tax framework since the 1940s." The department issued and finalized the drafts of the corporate tax rules in 2022.

"After several years of engagement with stakeholders, we are now beginning the formal SAPA rulemaking process," Ryan Cleveland of the tax department told *Tax Notes* August 9.

Public comments on the proposed regs must be submitted by October 10. The department noted that stakeholders had opportunities to comment during the development of the proposed regs.

'A Welcome Step Forward'

Ted Friedman, partner with Eversheds Sutherland (US) LLP, told *Tax Notes* August 9 that the release of the proposed corporate tax reform regs is "a welcome step forward."

"This is a day we've been waiting almost nine years for," Timothy P. Noonan, partner with Hodgson Russ LLP, told *Tax Notes* in an email. He said the department should be commended for its work to finalize the regs, particularly considering the chaos caused by the pandemic.

Both Noonan and Friedman noted that since the 2015 corporate tax overhaul, taxpayers were faced with regulatory uncertainty and often had to proceed without final guidance from the department. "That uncertainty has presented challenges for taxpayers," Friedman added.

Noonan said the formally proposed regs updated the rules on sourcing a corporation's receipts from passive investment customers, including income categories like hedge funds and private-equity management fees. He added that he and colleague Open Weaver Banks examined the sourcing rules for investment managers in an October 2022 *Tax Notes* column.

Instead of sourcing receipts from the customers to the location where the contract is managed by the passive investment customer, Noonan said the proposed regs now say that the "benefit of services provided to a passive investment customer is presumed to be received at *the location of the investors* in such passive investment customer, unless the investor is holding the interest in the passive investment customer for a beneficial owner."

“There will be some winners and losers here; some will like the new rule, others may not," Noonan said. "But at the very least, the change seems more in line with the idea behind market sourcing; the prior version ended up with a result that looked more like a 'where performed' apportionment rule."

Friedman said that the department’s draft corporate tax reform regs have received extensive feedback from tax practitioners and industry groups over the years. One item of note, Friedman said, is the department’s inclusion of provisions addressing P.L. 86-272, largely based on the Multistate Tax Commission’s model statute.

The department’s regulatory impact statement on the proposed regs outlined the positions taken by commenters.

“While some commenters advocated for the elimination of the additional rules for internet-based activities, arguing that rules of statutory construction do not support the Department's interpretation of Public Law 86-272, other commenters concluded that the Department has the authority to promulgate regulations that narrowly interpret the Public Law 86-272 protections, and should leave it to the courts to decide whether the Department’s interpretation is correct," the statement said, adding that the formally proposed regs contain guidance about P.L. 86-272’s application for corporations that conduct business over the internet.

A Closer Look

The proposed corporate tax reform regs, spanning more than 400 pages, repeal and replace parts 1 through 9 and parts 32 to 33 of the department’s corporate tax rules.

Part 1 includes updated rules on the state’s new economic nexus standard and guidance for corporations seeking protection under P.L. 86-272 and those invested in limited liability companies and partnerships.

Part 2, on accounting procedures, is "largely unchanged from its predecessor regulations," according to the department's overview of the regs.

Part 3 provides guidance on the computation of capital and business income and has been "substantially revised from the existing regulations due to statutory changes to the various types of income, capital, and losses," according to the department. Subparts 3-8 and 3-9 update the department’s treatment of net operating losses and NOL deductions.

Part 4 relates to business apportionment, including how to properly source sales of receipts from digital products (such as cryptocurrency) and digital services.

Part 5 relates to some tax credits, such as the investment tax credit, the employment incentive credit, and security training tax credit, and "incorporates statutory changes," according to the regs' overview.

Part 6 provides guidance on reporting requirements. Notably, amendments to subpart 6-2 reflect the corporate tax overhaul that made changes to combined reporting "by moving to a system that requires combination when a more than 50 percent ownership test is met and the corporations are engaged in a unitary business," the department said.

Part 7, on the payment of tax and estimated tax, contains technical and conforming amendments.

Part 8 details the computation of the metropolitan transportation business tax surcharge. It contains the surcharge rate in effect for tax years beginning on or after January 1, 2015, and before January 1, 2024.

Part 9 provides definitions pertaining to special entities such as qualified New York manufacturers, corporate partners, S corporations, real estate investment trusts, regulated investment companies, and domestic international sales corporations. Part 9 also reflects the changes that "merged the bank tax imposed under Tax Law article 32 into the corporate franchise tax imposed under article 9-A," according to the department's overview of the regs.

The proposed rules repeal parts 32 and 33. The proposed new Part 32 updates combined reporting requirements for insurance corporations.